



City of Carlsbad

Finance Department

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JUN 23 2008

THEASURER
STATE OF CALIFORNIA

June 18, 2008

Mr. Robert Grossman
Group Managing Director
U.S. Public Finance
FITCH RATINGS
33 Whitehall Street, 27th Fl.
New York, NY 10004

Ms. Gail Sussman
Group Managing Director
Public Finance
MOODY'S INVESTORS SERV.
250 Greenwich Street
New York, NY 10007

Mr. William Montrone
Head
U.S. Public Finance Dept.
STANDARD & POOR'S
55 Water Street
New York, NY 10041

SUBJECT: ENDING DOUBLE STANDARD IN RATINGS OF MUNICIPAL AND CORPORATE BONDS

Dear Mr. Grossman, Ms. Sussman, and Mr. Montrone;

The current system of assigning credit ratings to bonds issued by governmental entities which provide essential services to the public leads to indefensible market discrimination against state and local municipal issuers. The rating agencies' own studies show that the likelihood of default by municipal borrowers is much lower than for corporate borrowers with similar ratings. Ratings should be based primarily on an evaluation of the likelihood investors will suffer a loss due to default. Unfortunately, for municipal bonds, they are not. This practice costs taxpayers enormous amounts of money that could be invested in public programs and infrastructure.

The City Council of Carlsbad recently adopted a resolution (copy enclosed) urging your companies to end the double standard in the treatment of municipal and corporate bonds. The City Council urges you to treat taxpayers the same as corporations and rate municipal bonds based on the risk investor loss due to default. Finally, we urge you to do this by creating a unified, global rating approach that treats all issuers equally, thereby better serving taxpayers and investors.

Sincerely,

LISA IRVINE
Finance Director

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Enclosure

c: Ron Ball, City Attorney
Bill Lockyer, California State Treasurer



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RESOLUTION NO. 2008-135

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF
CARLSBAD, CALIFORNIA, SUPPORTING REFORM OF
THE BOND RATING SYSTEM TO ELIMINATE
DISCRIMINATION AGAINST MUNICIPAL BONDS**

WHEREAS, the recent turmoil in the municipal bond markets has brought into focus the higher standards imposed by the three major bond rating agencies in rating municipal bonds compared to corporate bonds, mortgage-backed securities and other debt instruments; and

WHEREAS, issuers of municipal bonds rarely default on the bonds they sell to finance streets and roads, public buildings, bridges, flood protection and water systems, and other critical infrastructure, yet municipal bond ratings fail to reflect that fundamental fact; and

WHEREAS, the rating agencies even acknowledge this disparity, but they ignore it in their ratings. Standard & Poor's for example, acknowledges that the historic rate of defaults of A-rated municipal bonds is 0.23 percent, while that of corporate bonds is 2.91 percent or 13 times greater; and

WHEREAS, despite the relative default rates shown by their own data, the rating agencies continue to discriminate against municipal issuers, requiring public agencies to secure expensive bond insurance in order to secure bond ratings comparable to those of private corporations; and

WHEREAS, the rating agencies base their ratings of corporate bonds on the risk the issuer will default. Their ratings of municipal bonds, in contrast, have little relationship to the risk of default. This difference provides a substantial economic benefit at the expense of the taxpayers across the nation; and

1 WHEREAS, a coalition of state and local public agencies, led by California
2 State Treasurer Bill Lockyer, has called on the three major rating agencies to examine
3 their practices and treat municipal bonds on par with corporate bonds that expose
4 investors to the same level of risk. The Treasurer also testified before the House
5 Financial Services Committee on March 12, 2008 about the need for reform; and

6 WHEREAS, the response by the rating agencies to call for reform has been
7 uneven, Moody's has taken the greatest strides, announcing it will assign a corporate-
8 equivalency rating (what it calls a global scale rating or GSR) alongside the traditional
9 municipal rating to any municipal bond at the issuer's request; and

10 WHEREAS, the current double-standard by rating agencies: (1) drains
11 billions of dollars from taxpayers in the form of unfairly high interest rates; (2) forces
12 taxpayers to pay even more money to buy bond insurance – insurance they would not
13 have to purchase if municipal bonds ratings accurately reflected the slight risk of default;
14 (3) misleads investors by grossly inflating the risk of buying municipal bonds; and (4)
15 undermines the effective function of a transparent market.

16 NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of
17 Carlsbad, California, as follows:
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- 20 1. That the above recitations are true and correct.
 - 21 2. That the City Council of the City of Carlsbad calls on the major municipal
22 bond agencies to end the double standard in the treatment of municipal and corporate
23 bonds; to treat taxpayers the same as corporations and rate municipal bonds based on
24 the risk of default; and to create a unified, global rating approach that treats all issuers
25 equally, and better serves taxpayers and investors.
 - 26 3. That the Finance Director is hereby directed to notify the municipal bond
27 rating agencies by letter of adoption of this Resolution, with a copy to California State
28 Treasurer Bill Lockyer and to register the City as a member of the coalition of public
agencies supporting the nationwide effort to reform how bond rating agencies grade
state and local bonds.
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1 PASSED, APPROVED AND ADOPTED at a Regular Meeting of the City Council
2 of the City of Carlsbad on the 13th day of May, 2008, by the following vote to wit:

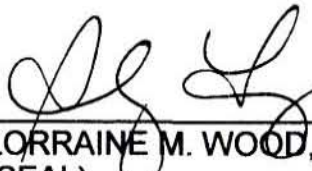
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4 AYES: Council Members Lewis, Kulchin, Hall, Packard and Nygaard.

5
6 NOES: None.

7
8 ABSENT: None.

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11 
12 CLAUDE A LEWIS, Mayor

13 ATTEST:

14
15  Deputy
16 LORRAINE M. WOOD, City Clerk
17 (SEAL)

